

NEW YORK CLEARING HOUSE

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JILL M. CONSIDINE
PRESIDENT

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11/17/98

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December 24, 1997

Ms. Cynthia L. Johnson
Director
Cash Management Policy
and Planning Division
Financial Management Service
U.S. Dept. of the Treasury
Room 420
401 Fourteenth Street, S.W.
Washington, D.C. 20227

Re: Electronic Payment of Federal
Disbursements (RIN 1510-AA56]

Dear Ms. Johnson:

The New York Clearing House Association¹ is pleased to comment once more on a proposal by Treasury Department to implement section 31001(x) of the Debt Collection Improvement Act of 1996 (the "Act"), which requires federal agencies to convert federal payments (other than payments under the Internal Revenue Code) to electronic funds transfers.² Treasury issued an interim rule on July 26, 1996,³ which will remain in effect through January 1, 1999. Although Treasury implemented the interim rule

¹ The members of the New York Clearing House Association are The Bank of New York, The Chase Manhattan Bank, Citibank, N.A., Morgan Guaranty Trust Company of New York, Bankers Trust Company, Marine Midland Bank, Fleet Bank National Association, European American Bank, and Republic National Bank of New York.

² 62 Fed. Reg. 48,713 (Sept. 16, 1997).

³ 61 Fed. Reg. 39,254 (July 26, 1996).

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without the usual delayed effective date, it did request comment on the interim rule and the responses to that request for comment were evidently helpful to Treasury in framing and resolving a number of critical issues it faced in preparing a proposed final rule to take effect upon the expiration of the interim rule in January 1999. The Clearing House commented on issues related to the interim rule,⁴ and we are pleased to see that Treasury has adopted an approach that is consistent with that recommended by the Clearing House in its comment letter.

The Clearing House strongly supports the Act and Treasury's efforts to implement it in a rapid, straightforward fashion. Electronic payments are clearly superior to payments made by check, and the recipients of federal payments, as well as the federal government, will benefit greatly by moving away from paper-based systems and toward electronic payments.

Some of the benefits of EFT payments are:

- Greater security from theft and fraud. Electronic payments cannot be lost or stolen.
- Faster availability. Under Federal Reserve regulations and rules of the National Automated Clearing House Association, electronic payments receive same-day availability. There is no delayed availability for electronic payments.
- Cost-effectiveness. Shifting to electronic payments will save the federal government approximately \$100 million per year, and for the

⁴ Letter from Jill M. Considine to Cynthia L. Johnson (Nov. 26, 1997).

overwhelming number of recipients the change will not result in any additional charges. In fact some banks charge customers for check deposits, but we are not aware of any banks that charge for credits received through an automated clearing house, the method of choice for direct deposit of small-dollar payments.

While some have expressed concern that a shift to electronic payments will result in added costs for some groups, this will not be the case for an overwhelming majority of recipients of federal payments. The Treasury Department's briefings to the banking industry have clearly demonstrated that Treasury has done extensive studies of the effects of the new requirements on various groups and is in full possession of the relevant facts. Treasury should make these facts known to the wider public so that those who are concerned about increased cost may be put at ease.

The balance of this letter will address individually the most significant issues raised by the Treasury's proposal.

Authorized Payment Agent

Section 3332(g) of 31 U.S.C. requires recipients of federal payments to designate one or more financial institutions or other authorized agents to receive payments. The Act does not define the term "authorized payment agent," nor does the legislative history provide much guidance. A threshold issue for Treasury therefore is: Which persons or institutions should be authorized to act as agents for receipt of electronic payments for the benefit of recipients? Treasury appears to have received numerous comments on this issue urging that it adopt one or another alternative: Some consumer organizations recommended that

only financial institutions and the U.S. Postal Service be permitted to act as authorized payment agents; check cashers and money transmitters urged that their organizations be permitted to act as authorized payment agents.⁵

Treasury has chosen a conservative approach. In all cases payment will be made to an account at a financial institution that is in the name of the recipient or in the name of an authorized agent who "stands in the shoes of the recipient for purposes of payment."⁶ Such a person must be an individual or entity appointed or otherwise selected as a representative payee or fiduciary under regulations of the Social Security Administration, the Department of Veterans Affairs, the Railroad Retirement Board, or other agency.⁷

The Clearing House supports Treasury's approach. Treasury is rightly concerned about delivering payments to third parties that are not subject to federal supervision or consumer protection laws and about the possibility that the third parties would not honor their obligations to pay the recipients. Third parties will be permitted to receive federal payments for recipients who are mentally or physically incapable of managing their payments and for whom a payment agent or fiduciary has been appointed under existing regulations of the Social Security Administration, the Department of Veterans Affairs, or similar agencies. These agencies have issued regulations addressing the qualifications and duties of these payment agents. These are well-established programs that have proved their usefulness to recipients who are not capable of managing their payments, and

⁵ 62. Fed. Reg. at 48,716.

⁶ Id. at 48,717.

⁷ Proposed 31 C.F.R. § 208.2(b).

these agencies have the controls necessary to prevent abuse. We believe that exceptions in these situations are warranted and that the restrictions that Treasury has proposed are appropriate to ensure that the interest of the recipients are protected.

Waivers

The Act authorizes Treasury to waive the requirement for electronic payment under certain circumstances. Treasury solicited comment on the need for waivers. In response to the comments, Treasury has developed some general rules:

1. No waivers will be given for persons with accounts at financial institutions who become eligible for federal payments after July 26, 1996.
2. Persons who have accounts at financial institutions who became eligible for federal payments before July 26, 1996, may continue to be paid by check if they certify that the use of electronic payments would create a hardship because of physical disability or a geographic barrier.
3. Individuals without bank accounts may still be paid by check if the use of electronic payments would create hardship because of physical disability, geographic barriers, or if use of EFT would cause a financial hardship. Moreover, persons without bank accounts have an automatic waiver until January 2, 2000, or until the account that Treasury plans to have for the unbanked becomes available.

Other waivers will be available for payments to recipients in countries where electronic payments are not available, when

natural or other disasters make electronic payments difficult or impossible, in theaters of military operations, and for law-enforcement or national-security purposes where the payment by electronic means would not be advisable because, for example, it could jeopardize the life of a confidential informant.

The Clearing House believes that Treasury has made a reasonable compromise between the twin goals of converting as many payments as possible to electronics and not imposing undue hardships on individuals or impeding other legitimate governmental goals. Most of the exceptions (e.g., those for sensitive law-enforcement payments, military theaters, and the like) are entirely appropriate. We believe that it is also appropriate to distinguish those without bank accounts from those with accounts and to distinguish further those who became eligible for federal payment before the Act took effect and those who became eligible afterward. Ideally, no one with a bank account would be exempt from the electronic payment requirement. We understand, however, that some persons who are used to receiving paper checks may be apprehensive about the change, especially in light of some of the inaccuracies regarding direct deposit that have been reported in the press. Under these circumstances, we believe that it is appropriate to grant the limited hardship waiver outlined in the proposal and grant those waivers based on the declaration of the persons making the request. We also believe that it would be appropriate to revisit the topic of waivers for persons with banks accounts at some point in the future when recipients become more familiar and comfortable with electronic payments.

Persons Without Accounts

The unbanked raise different, more difficult questions. We agree that the primary goal should be to move the unbanked into

the financial mainstream, but we also understand that this may not be feasible for large numbers of the unbanked and that some alternatives must be made available to them.

Commenters addressing this difficult issue suggested several alternatives. Some recommended that Treasury require banks and other depository institutions to open accounts for the unbanked that would provide basic banking services at little or no cost. Treasury has determined that "financial institutions should not be required to provide these types of accounts as a result of the Act."⁸

The Clearing House agrees completely with Treasury on this point. There is nothing in the Act or its legislative history to suggest that Congress intended to mandate these "basic banking" or "lifeline" accounts. Several states have adopted requirements of this sort, but in practice these accounts have not generally worked very well: the fees that banks are limited to are frequently insufficient to cover the costs of providing the accounts, and the accounts frequently attract people who do not need low-cost services. Private-sector businesses should not be forced into unwanted relationships, especially where the terms mandated for these relationships are such that the relationship will most likely result in loss.

There is a wide-spread belief that the electronic payment mandate will result in a windfall for banks because they will be able to open millions of new accounts and receive billions of dollars in new deposits from which they will make enormous profits just from float management. This is simply not the case. In the first place, the days of making significant profits from float management are gone, a victim in part of the general

⁸ 62 Fed. Reg. at 48,721.

decline of interest rates over the past decade. Secondly, any new accounts for the unbanked will not result in significant amounts of idle funds that banks can invest. For the most part, the unbanked are economically disadvantaged and have a pressing need for cash. Experience with these kinds of accounts indicates that the holders will draw down their balances almost as soon as the deposits are made. This means that very little, if any, of these deposits will remain on balance for very long; typically the account balance will be reduced to zero well before the next deposit is made. The result is that these accounts simply will not provide significant idle funds that banks can reinvest; float income for these accounts will be negligible, certainly not nearly enough to cover the costs of servicing these accounts, including accounting for deposits and withdrawals, generating statements, and responding to inquiries.

Treasury also rejected a second approach: developing a model account that financial institutions would be invited to offer to the unbanked at a specific price. We agree with Treasury that this would require the development of a regulatory infrastructure and could still result in services being unavailable in some parts of the country.

Treasury has chosen to follow a third approach: "engage one or more Federally-insured depository institutions to act as Treasury's financial agent for the provision of accounts to [the unbanked]."⁹ Treasury plans to develop an account, specifying the terms and conditions that will apply. It will choose one or more agents on the basis of a competitive process. The Clearing House believes that Treasury has chosen the best alternative. No institution will be forced into unprofitable relationships, but any bank may seek to provide the service through an arrangement

⁹ Id.

December 24, 1997

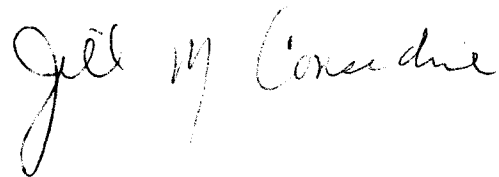
with Treasury. This approach will provide the best chance that the unbanked will be able to have access to their funds and gain the benefits of electronic payments, but that no financial will be coerced into providing services on terms that to which it would not ordinarily agree.

* * * * *

To summarize, the Clearing House believes that Treasury has generally made the right choice among the options open to it in a difficult and complex field. We support the Treasury's proposed final rule and look forward to working with Treasury in the rapid implementation of the EFT 99 mandate.

If you have any questions, please call Joseph R. Alexander, Counsel, at (212) 612-9334.

Very truly yours,

A handwritten signature in cursive script, reading "Jill M. Conedine". The signature is written in dark ink and is positioned below the typed name "Jill M. Conedine".

JMC:mlr